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ONE COUNTRY, TWO SYSTEMS: HONG KONG'S PARADOX OF POLITICS AND BUSINESS

. . . and now he was going ashore to witness the formality of taking possession, to watch a Chinese island become a jewel in the crown of her Britanic Majesty, Queen Victoria.

Taipan by James Clavell

Hong Kong has been revitalized. The Sino-British Joint Declaration, initialed September 26, 1984,¹ set in motion political forces which, it is hoped, will maintain Hong Kong's economic system and way of life through July 1, 2047. Until then, July 1, 1997 marks the date when the British government will transfer one of its remaining colonies directly to a communist state.²

Under the leadership of Deng Xiaoping, China has adopted a political philosophy of "one country, two systems."³ It is hoped that this philosophy will allow Hong Kong to continue its capitalist economy under socialist rule. In essence, Hong Kong's political future is viewed as functioning as a regional government within a unitary system.⁴ While under British rule, Hong Kong has successfully prospered as a result of the impartial liberal economic philosophy of "positive noninterventionism."⁵ As negotiations over Hong Kong's future appeared plagued with ideological differences, the colony's economy noticeably faltered.⁶ Since the signing of the Joint Declaration, however,

1. Joint Declaration of the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the People's Republic of China on the Question of Hong Kong, Dec. 19, 1984, United Kingdom-People's Republic of China, 1984 Gr. Brit. T.S. No. 20 (Cmd. 9352) [hereinafter Joint Declaration]; reprinted in 7 LOY. L.A. INT'L & COMP. L.J. 141 (1984).

2. *More Fears Than Cheers In Hong Kong*, EUROMONEY, April 1985, at 151.

3. *Id. Perhaps, Perhaps, Perhaps* . . . , ECONOMIST May 11, 1985, at 3. A high ranking Chinese official has stated that the expression "one country, two systems" contains "no contradiction," and added that the concept "proceeds from the actual conditions of Hongkong and Taiwan." It is a development of Marxism-Leninism and a "concrete manifestation of building socialist Chinese characteristics." R. Delfs & M. Lee, *Correct Ideology for Home Consumption*, FAR EAST. ECON. REV., Dec. 5, 1985, at 14, col. 3.

4. Harding, *The Future of Hong Kong*, CHINA BUS. REV., Sept.-Oct. 1985, at 36, col. 1.

5. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 4.

6. For example, between January and December of 1982, Hong Kong's stock exchange index, the Hang Seng, was halved. *Hong Kong Future*, ECONOMIST, Mar. 12, 1983, at 52. Hong Kong's real estate market experienced a similar collapse as more than a

Hong Kong's economy has experienced a slow and continuous upsurge. Despite the currently improving economic climate, which has resulted from China's recent liberalized economic policies in the world market, the Chinese government is committed to its goal of building socialism.⁷

This Note examines the historical background which has led to Hong Kong's present political situation. It will highlight the provisions of the Joint Declaration that many believe will greatly affect the economic functioning of the Island. Opposing views concerning the advisability of investment in Hong Kong today will also be examined. The political climate and its impact on the business community will be given considerable attention.

I. HISTORICAL PERSPECTIVE

Britain's possession of Hong Kong was the culmination of not one, but three treaties signed with China in the nineteenth century. Between 1839 and 1842, China attempted to enforce its laws to halt the profitable opium trade that supplied Great Britain with the capital necessary to pay for China's goods.⁸ The attempt by China to enforce its laws precipitated the Opium War.⁹ One result of this conflict was the Convention of Chuanbi in 1841, through which an attempt was made to cede Hong Kong Island to Britain.¹⁰ Both the British and Chinese governments were dissatisfied with the agreement's terms and refused to ratify it.¹¹ Hostilities again resumed, but this time the war was brought to an end with the signing in 1842 of the Treaty of Nanking,¹²

dozen small property companies failed as a result of falling land prices and rents. *Re-Investing Optimism*, *ECONOMIST*, Nov. 12, 1983, at 93.

7. R. Delfs & M. Lee, *supra* note 3, at 15, col. 1.

8. BRITISH INFORMATION SERVICES, HONG KONG, No. 80/84, Classification 7(b), at 6 (Oct. 1984) [hereinafter HONG KONG].

9. China grew increasingly concerned about its trade deficit with Great Britain which was largely attributable to Britain's trafficking of opium onto the mainland. To rectify this trade imbalance, China seized British trading factories and opium inventories in Canton and other outposts. The Opium War (1839-1842) promptly arose from this attempt by China to control the illicit opium trade, and essentially transformed China into a semi-feudal and semi-colonial country with "consequent loss of independent control over foreign trade." CHINA HANDBOOK SERIES, *ECONOMY* 388 (1984) [hereinafter *ECONOMY*]. For additional information on the causes of the war, see W. BEAGER, *THE COMMERCIAL FUTURE OF HONG KONG*, 11-16 (1978); Note, *The Legal Implications of the Sino-British Treaties Regarding Hong Kong*, 4 *LOV. L.A. INT'L & COMP. L.J.* 111, 111-12 (1981) [hereinafter *Sino-British Treaties*].

10. HONG KONG, *supra* note 8, at 6.

11. *Id.*

12. Treaty of Nanking, Aug. 29, 1842, China-Great Britain, 30 *British and Foreign State Papers* 389, reprinted in 93 *Parry's T.S.* 465 (1979).

resulting in China having ceded Hong Kong to Britain in perpetuity.¹³ In 1860, the Convention of Peking terminated further hostilities between Britain and China and secured to the British Crown the cession, in perpetuity, of the southern part of the Kowloon Peninsula and Stonecutter Island.¹⁴ Hong Kong's boundaries were extended once again in 1898 in order that Britain would be able to properly protect its new avenues of trade. The Convention of 1898¹⁵ effectuated such protection by authorizing a 99-year lease of the New Territories.¹⁶ The 1898 agreement itself "recognized that an extension of [the] Hong Kong territory [was] necessary for the proper defense and protection of the Colony."¹⁷

It was this lease of the New Territories, with a fixed expiration date, that prompted the British Government to attempt to enter into negotiations with China on the future of the Hong Kong territories.¹⁸

Following World War II, Hong Kong's economy flourished. By 1949, the Communists had come into power and established the People's Republic of China (China). Under the leadership of Mao Tse-tung, the Communists focused on the problems of the Chinese peasantry,¹⁹ leaving Hong Kong's capitalist economy and industry alone to mature.²⁰ In rhetoric, however, Chinese authorities continuously condemned Britain's presence in Hong Kong, arguing that the three trea-

13. Hong Kong was ceded to Britain as an indemnity for all the opium seized by China during the War. Day, *The Recovery of Hong Kong by the People's Republic of China—A Fifty Year Experiment in Capitalism and Freedom*, 11 SYR. J. INT'L L. & COM. 625, 630 (1984).

14. Convention of Peking, Oct. 24, 1860, China-Great Britain, 50 British and Foreign State Papers 10, reprinted in 123 Parry's T.S. 71 (1979).

15. Convention with China Respecting an Extension of Hong Kong Territory, June 9, 1898, China-Great Britain, 90 British and Foreign State Papers 17, reprinted in 186 Parry's T.S. 310 (1970); P. WESLEY-SMITH, *UNEQUAL TREATY, 1898-1997* (1983).

16. The New Territories comprise ninety-two percent of the total land area under the control of the British Crown. HONG KONG, *supra* note 8, at 1.

17. 186 Parry's T.S. 310; see also P. WESLEY-SMITH, *supra* note 15, at 1, 11. "While the stated original purpose of the acquisition of the New Territories was for defense, they were, in fact assimilated into the commercial life of the colony" that already developed under the laissez-faire policies of the colonial administration. Day, *supra* note 13, at 630.

18. HONG KONG, *supra* note 8, at 1. Thus, Hong Kong actually refers to Hong Kong Island, Kowloon and the New Territories. Note, *Legal Aspects of the Sino-British Draft Agreement on the Future of Hong Kong*, 20 TEX. INT'L L.J. 167, 169 (1985) [hereinafter *Legal Future of Hong Kong*].

19. To make amends for China's past century of "degradation" and to create a "self-sufficient egalitarian China," Mao understood that he had to look to the Chinese masses and improve their lives. *Sino-British Treaties*, *supra* note 9, at 112-13. The slogan "Serve the people" signified Mao's social aim to serve the collective good. *Id.* at 113.

20. *Id.* at 112.

ties of the nineteenth century were void as unequal.²¹ As a result, since 1949 China has often made claims that Hong Kong is actually a Chinese territory. In 1972, the Chinese ambassador, Huang Han, stated that "Hong Kong and Macao are part of Chinese territory occupied by the British and Portuguese authorities. The settlement of the question of Hong Kong and Macao is entirely within China's sovereign right and does not at all fall under the category of colonial territories."²²

Hong Kong also saw its population grow immensely following World War II. This boom in population was due to the return of many Chinese who fled the Japanese invasion during the war,²³ and the arrival of an additional 700,000 refugees²⁴ from the subsequent Chinese civil war.²⁵ By 1956, Hong Kong's population grew to two and one half million.²⁶

During the Korean War, Hong Kong experienced economic stagnation as a consequence of the United Nations embargo on Chinese goods from the People's Republic.²⁷ Following this lull in economic prosperity, Hong Kong underwent an economic surge primarily founded upon textiles²⁸ manufactured for export, as well as the manufacture of watches, clocks, toys, plastic goods and electronic products.²⁹

As a result, Hong Kong's economy has continued, since the 1950's, to be based upon export-promoting industries. This emphasis on exportation seems to be a most natural occurrence in light of the fact that Hong Kong maintains probably the most modernized and accessible harbor on China's coast.³⁰ China's awareness of the value of Hong Kong's harbor and access to international markets is reflected by the fact that Hong Kong is China's number one source of foreign currency earnings as well as its largest port of re-exportation.³¹ This dependence

21. *Legal Future of Hong Kong*, *supra* note 17, at 169. For a discussion of international law concerning unequal treaties, see *infra* notes 36-39 and accompanying text.

22. J. COHEN & H. CHIU, *PEOPLE'S CHINA AND INTERNATIONAL LAW: A DOCUMENTARY STUDY* 384 (1974).

23. *HONG KONG*, *supra* note 8, at 7.

24. Day, *supra* note 13, at 631.

25. *HONG KONG*, *supra* note 8, at 7.

26. G. ENDACOTT, *A HISTORY OF HONG KONG* 310 (2d ed. 1973).

27. *HONG KONG*, *supra* note 8, at 7.

28. Many mainland Chinese who sought refuge in Hong Kong during the Korean War were capitalists from Shanghai who established the textile industry that exists today. Day, *supra* note 13, at 631 n.41.

29. *HONG KONG*, *supra* note 8, at 7.

30. W. BEAZER, *THE COMMERCIAL FUTURE OF HONG KONG*, 1 (1978).

31. *ECONOMY*, *supra* note 9, at 399. Re-exports are those goods assembled in Hong Kong from components made elsewhere and subsequently exported once again. A. Ignatius, *Hong Kong's Premier Capitalist Roaders Are Emerging as Peking's Trusted Allies*, *Asian Wall St. J.*, Jan. 27, 1986, at 16, col. 4. The importance of Hong Kong to China's

on Hong Kong's capitalist structures will only help to assure the international community of the communist commitment to adhere to the provisions of the Joint Declaration signed with Britain in December of 1984.³²

II. PARTICULARS OF THE JOINT DECLARATION

The Joint Declaration signed between China and Great Britain was an eagerly awaited event in the international business community. It served to provide some indication to the community that their investments in Hong Kong would be preserved when the Island's sovereignty reverts back to China on July 1, 1997. The Joint Declaration itself consists of a joint declaration, three annexes and two brief memoranda exchanged between the two countries. The annexes include an elaboration by the Chinese Government of its basic policies regarding Hong Kong; the establishment of a Sino-British Joint Liaison Group; and a discussion on the question of land leases.³³ The memoranda discuss the citizenship status of those persons who are domiciled on the Island.³⁴

An elaborate discussion of the provisions contained within the Agreement is unnecessary because of the numerous articles that have already been written concerning the details of the document.³⁵ Necessary insight, however, will be provided by emphasizing those elements of the Joint Declaration that will, in all probability, have an impact on the economic status of Hong Kong and foreign investment.

Of particular relevance is that the legal controversy concerning the

export trade is enormous. In 1984, Chinese goods sent to Hong Kong accounted for one-third of the foreign currency earnings of China; and one half of the export commodities originating from the mainland are re-exported to foreign countries through Hong Kong. *ECONOMY*, *supra* note 9, at 399. Other sources have stated that since the 1960's approximately forty percent (not thirty percent) of China's foreign currency exchange has come from Hong Kong. Day, *supra* note 13, at 632; *see also* Iyer, *Making a Deal for 1997*, *TIME*, Aug. 13, 1984, at 25.

32. To clarify matters: The Joint Declaration was initialed by its negotiators on September 26, 1984; it was later signed by British Prime Minister Margaret Thatcher and Chinese Premier Zhao Ziyang on Dec. 19, 1984. The agreement was then finally ratified by both countries on May 27, 1985, and registered with the United Kingdom on June 1, 1985. Harding, *supra* note 4, at 32-33.

33. *See* Joint Declaration, *supra* note 1.

34. *Id.*

35. *See generally* *Legal Future of Hong Kong*, *supra* note 17, at 170-81; Note, *The Reversion of Hong Kong to China: Legal & Practical Questions*, 21 *WILLIAMETTE L.J.* 327, 333-37 (1985) [hereinafter *Reversion of Hong Kong*]; Mushkat, *The Transition from British to Chinese Rule in Hong Kong: A Discussion of Salient International Legal Issues*, 14 *DEN. J. INT'L L. & POL'Y* 171 (1986).

validity of the Convention of 1898, which occasioned the lease of the New Territories to Britain, is now moot.³⁶ Both countries have entered into the Joint Declaration of 1984 on equal footing, and as such, it is binding upon both signatories.³⁷ Sir Geoffrey Howe, British Secretary of State for Foreign and Commonwealth Affairs, as well as a key negotiator of the final resolution, stated on the day the Joint Declaration was initialed that "we have enshrined the results of our negotiations in an international agreement *binding in all its parts*."³⁸ Howe later added that, "this is a formal, legally binding agreement, the highest form of commitment that can be entered into between two sovereign states."³⁹

36. China adheres to the accepted principle of international law that unequal treaties are not legally binding because they do not fulfill the requirement of sovereign equality between contracting parties. M. McDUGAL & W. REISMAN, *INTERNATIONAL LAW IN CONTEMPORARY PERSPECTIVE* 1177 (1981). Thus, China considers many of the nineteenth century treaties it has entered into as "unenforceable, because of duress and the unequal position of China in relation to the Western powers." *Reversion of Hong Kong*, *supra* note 35, at 330. The traditional Western view that a country is bound by its treaties despite duress or inequality of position has been modified by the 1969 Vienna Convention on the Law of Treaties, May 22, 1969, art. 52, 8 I.L.M. 679, U.N. Doc. A/Conf. 39/37, which voids any treaty procured by the threat or use of force. *Id.* Although China views as void and unequal the treaties which ceded Hong Kong and the new Territories to Great Britain, see *supra* notes 12-17, the Vienna Convention adds little substance to its argument. This is because a) the Vienna Convention does not apply retroactively, *Reversion of Hong Kong*, *supra* note 35, at 330; and b) the principle that as long as force is considered a "licit activity," duress and coercion can not be invoked to invalidate a treaty, McDUGAL & REISMAN, *supra* at 1178. It follows that China's attack on the inequality of the three nineteenth century treaties is futile since in Britain's view, and that of the rest of the Western world, the treaties are considered "lawful at the time of conclusion." See *id.*

The Chinese thus perceived the Joint Declaration as a renegotiation with Great Britain as an equal, of the three unequal treaties of the nineteenth century. *Legal Future of Hong Kong*, *supra* note 17, at 186. This renegotiation follows China's political philosophy that an affirmation of an unequal treaty or a replacement of it by a new agreement between independent and equal sovereign states adds legality to a practical situation not previously governed by rules of international law. P. WESLEY-SMITH, *supra* note 15, at 186-87. While not recognizing the validity of an unequal treaty, China's determination to abrogate one is based on political not legal considerations. *Id.* at 186.

37. This commitment is clearly set forth by both countries in the last clause of the Joint declaration itself: "This Joint declaration and its Annexes shall be equally binding." Joint Declaration, *supra* note 1, para. 8.

38. Address by Sir Geoffrey Howe, Press Conference in New York City (Sept. 26, 1984) (emphasis added) (available from British Information Services).

39. *Id.* One commentator has stated that the problems of Hong Kong in the earlier part of the century were partly the result of the inequality of the contracting parties of 1898: "[A]n unequal treaty is not the most reliable and secure basis for the transfer of territory and its subsequent administration." P. WESLEY-SMITH, *supra* note 15, at 188. If this is a valid argument, and if the Joint Declaration is viewed by both parties as truly

Despite the strong language used by Howe, Hong Kongers themselves have in the past voiced concern as to whether China will honor the Agreement.⁴⁰ This concern led some members of Hong Kong's executive council to request the British Parliament to state that the transfer of sovereignty will not be automatic but dependent on full implementation of the guarantees in the Agreement.⁴¹

The Joint Declaration at its outset officially declares the reversion of the Hong Kong area from Britain's to China's sovereign control effective July 1, 1997. It then establishes Hong Kong as a Special Administrative Region (SAR) in accordance with the provisions of Article 31 of the Chinese Constitution.⁴² The SAR will be under the direct control of China but will maintain a high degree of autonomy.⁴³ The Agreement also provides that China will promulgate and enact a Basic Law of the SAR consistent with the Chinese Constitution.⁴⁴ Of extreme significance is China's concession that this Basic Law shall stipulate that "the socialist system and socialist policies shall not be practiced in . . . Hong Kong" and that "Hong Kong's previous capitalist system and life-style shall remain unchanged for 50 years."⁴⁵

An inherent conflict arises within the provisions establishing the SAR and the accompanying Basic Law. Specifically, how can China promulgate and enact a Basic Law which attempts to be consistent with its Constitution and at the same time not endorse any socialist practices, especially since China's constitution is itself a communist document? This question must be resolved when China eventually drafts the SAR's Basic Law.⁴⁶ One fear is that China will intentionally

binding then the unequal treaties of the past pose no threat to Hong Kong's future sovereignty. See also *supra* note 6.

40. *Oh, All Right, Says Hong Kong*, *ECONOMIST* Dec. 1, 1984 at 44.

41. *Id.*

42. Joint Declaration, *supra* note 1, at para. 3(1). Article 31 stipulates that "the state may establish special administrative regions when necessary. The system to be instituted in special administrative regions shall be prescribed by law enacted by the National People's Congress in light of the specific conditions." PEOPLE'S REPUBLIC OF CHINA CONST. art. 31 (1980).

43. *Id.* para. 3(2). Hong Kong's foreign affairs and defense, however, will be the responsibility of China.

44. *Id.* Annex I, Section I. This Basic Law, to be enacted by the National People's Congress in Peking, will become Hong Kong's constitution, replacing the Letters Patent and the Royal Instruction of the British colonial system. *Oh, All Right, Says Hong Kong*, *supra* note 40, at 43.

45. Joint Declaration, *supra* note 1, at Annex I, Section 1.

46. The first draft is not expected to be completed before 1990. *Oh, All Right, Says Hong Kong*, *supra* note 40, at 43. One commentator has stated that "it will be hard to find a formula of words that does not leave Hong Kong believing that it will be more tightly controlled from Peking than it thought the settlement meant it to be." *Perhaps*,

make the wording of the Basic Law ambiguous, which will offer an opportunity for China to undermine Hong Kong's legal system in the future.⁴⁷ It is unquestioned that the framework of the Basic Law is a critical factor in attracting foreign investment in the future.⁴⁸ Any existing Hong Kong law that will in any way conflict with the Basic Law will be automatically deemed unconstitutional.⁴⁹

Of more immediate concern, especially in attracting a new flow of foreign currency into Hong Kong, is the Agreement's provisions that Hong Kong's social and economic conditions shall remain unchanged. The SAR will decide its own economic and trade policies.⁵⁰ Specifically, the Joint Declaration provides that "[p]rivate property, ownership of enterprises, legitimate right of inheritance and foreign investment will be protected by law."⁵¹ The agreement also assures that the Hong Kong SAR will retain its status as a free port and as an international financial center.⁵² "There will be a free flow of capital."⁵³ Personal rights and freedoms will be preserved including "those of the person, of speech, of the press, of assembly, of association, [and] of travel," among others listed.⁵⁴

Perhaps, Perhaps . . . , *supra* note 3, at 9.

47. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 9. See *infra* notes 80-103 and accompanying text for a discussion of problems confronted when interpreting the Joint Declaration.

48. *The Crucial Confidence Factor*, EUROMONEY, APR. 1985, at 162; see also *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 9.

49. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 9.

50. Joint Declaration, *supra* note 1, at paras. 3(9) and 3(10) (Hong Kong may participate in any international organizations and international trade agreements the SAR chooses to enter, and may develop economic and cultural relations with relevant international organizations).

51. *Id.* para. 3(5).

52. *Id.* para. 3(6) and 3(7). Hong Kong is currently the third largest financial center in the world.

53. *Id.* para. 3(7).

54. *Id.* para. 3(5). Although China has not yet fully made its new presence in Hong Kong felt, and despite assurances in the Joint Declaration, the free press has almost reflexively begun to check itself. Most notably, it was reported by journalists and academics that during 1985, editorials were less critical of China. Leung, *Hong Kong Press, Fearful of Reprisals, is Taking a Softer Line Toward Peking*, *Asian Wall St. J. Weekly*, Jan. 13, 1986, at 20, col. 1. It is believed by those in the profession that this spreading self-censorship, *id.* at 20, col. 4, is caused by fear that harsh criticism of China will be retaliated by Peking by not consulting Hong Kong on its future. *Id.* at 20, col. 2. But 1986 has brought new hope to the true meaning of free expression in Hong Kong. The *South China Morning Post* (the "Post"), Hong Kong's largest circulating English-language paper, has recently had a shake-down of its management. Gupta, *New Editor Sparks Acrimony While Reshaping The Media Backbone of Colony Establishment*, *Asian Wall St. J. Weekly*, Oct. 6, 1986, at 16, col. 1. With a controversial new Australian editor, the *Post's* editorials now attack both British and Chinese policies which were only

A Joint Liaison Group will also be set up by terms of the Agreement. The functions of the Joint Liaison Group are threefold: it shall "(a) conduct consultations on implementation of the Joint Declaration; (b) . . . discuss matters relating to the smooth transfer of the government in 1997; [and] (c) . . . exchange information and conduct consultations on such subjects as may be agreed by the two sides."⁵⁵

Under Annex III, which addresses the issue of land leases, all leases of land, granted before or after the Joint Declaration is in force, that extend beyond June 30, 1997 "shall continue to be recognized and protected."⁵⁶ The Agreement also permits the British Hong Kong Government to grant new leases until June 30, 1997 as long as they expire no later than June 30, 2047.⁵⁷

Leases of land, without a right to renewal, that expire after June 30, 1997 are to be dealt with in accordance with the land laws and policies of the SAR.⁵⁸ In October of 1985, it was reported that more than 30,000 New Territory leases which simultaneously expire in June 1997 might be renewed by one act of special legislation.⁵⁹ An effective and efficient mechanism for land lease renewals is a crucial element to ensure Hong Kong's future prosperity. The Island cannot expect to attract long term foreign investments without assuring the protection of property interests. Thus, if the 30,000 New Territory leases are renewed by the SAR, it will help provide an impetus to attract foreign

recently viewed by newspapers as off-limits. *Id.* The new editor has reserved the right to criticize any government and described the *Post* as "standing for more democratization" in Hong Kong. *Id.* at 16, col. 3. Most recently, the *Post* strongly criticized China's arrest on July 17, 1986 of the New York Times reporter John Burns (whom Peking accused of spying), and the joint Chinese-Hong Kong venture to build a nuclear power plant only 20 miles from the Hong Kong border so soon after the Chernobyl disaster in the Ukraine. *Id.* All this change in editorial conservatism comes at a time when the *Post* is considered the most profitable newspaper in Hong Kong, if not the world. *Id.* at 16, col. 1.

55. *Id.* Annex II, para. 3. The Joint Liaison Group is not to pursue an active or even supervisory role in the administration of the SAR. It will be essentially a monitoring body. The Joint Liaison Group shall consist of a senior representative and four other members, from each country.

56. *Id.* Annex III, para. 1.

57. *Id.* Annex III, para. 2. The total amount of new land that the British Hong Kong Government may lease under Annex III is limited to 50 hectares a year.

58. *Id.*

59. Telex to the Commissioner for Hong Kong Commercial Affairs (Oct. 1985).

Hong Kong Standard reports . . . that more than 30,000 New Territories leases which will expire in June 1997 may be renewed in one go by special legislation. The paper says this is one of the options being seriously considered by senior officials in the lands department who are looking for a cost-effective way to deal with the extension.

Id.

capital.

Of related importance to the securing of property interest, is the unanswered question concerning a number of 999-year leases, many of which are held by the Hong Kong Land Company. The explanatory notes to the Joint Declaration give assurances that interest in the 999-year leases will be protected.⁶⁰ The clauses dealing with land leases, however, state only that such leases will be protected under Hong Kong law until 2047.⁶¹

Despite the noted ambiguities of the Joint Declaration itself, one fact remains unquestioned: since the initialing of the Agreement in September of 1984, Hong Kong has been experiencing an economic revival.

III. A NEW ECONOMIC SURGE AMID POLITICAL RUMBLINGS

The superiority of the socialist system in China has yet to be brought into full play . . . due in great part to a rigid economic structure that cannot meet the needs of the growing forces of production. Top priority over the next five years will be reforms in the industrial economics of urban centers to include rationalization of pricing system, local autonomy, a flexible planning system, great material incentives and bonuses for the workers, the encouragement of competition, and an expansion of foreign participation and investment in the Chinese economy.⁶²

This excerpt from the third plenary session of the Central Committee of the Communist Party of China, released between the initialing and signing of the Joint Declaration, firmly conveys China's intentions concerning its future economic policy. From this economic forecast, it appears that Hong Kong will be one of its greatest beneficiaries.

Aside from this rhetoric, the central issue remains whether the future economic success of Hong Kong as a world financial center will continue, and whether "the rest of the world will accept China's assurances that, after the British withdrawal, the banking, currency and commercial institutions will remain undisturbed and completely under Hong Kong management."⁶³

60. *The Details At Last*, *ECONOMIST* Sept. 29, 1984, at 35.

61. *Id.* See also Joint Declaration, *supra* note 1, at Annex III.

62. Holden, *China Goes Capitalistic*, 96 *U.S. BANKER* 47 (1985).

63. *The Art of Staying Central*, *EUROMONEY*, Apr. 1985, at 164.

A. *The Pessimists*

When signing the Sino-British Joint Declaration, senior Chinese Communist Party officials were concerned that foreign bankers might not favor taking the risk of being supervised by the Chinese Communist Party.⁶⁴ This may have been precipitated by a realization by some Chinese officials of the complexities inherent in drafting Hong Kong's Basic Law in a manner free from socialist doctrines yet consistent with the Chinese Constitution.⁶⁵

Since Mao launched his Cultural Revolution in 1966, there has been a deep mistrust instilled in Hong Kong businessmen of China's true intentions concerning the territory. This feeling of mistrust has been a factor in every subsequent business consideration.⁶⁶ Although the force of this distrust may be questioned since it is not measurable, it remains to be seen whether the individuals who have turned Hong Kong into East Asia's most successful export manufacturing center and financial market will be convinced that "they have a bright future under Beijing's sovereignty."⁶⁷

China also undertook some "contingency planning" during the Sino-British negotiation. China's studies of the Hong Kong situation included "an assessment of how much Beijing would lose if a collapse of confidence undermined the territory's economy."⁶⁸ The results were not favorable for the Hong Kong entrepreneurs who wanted to believe in China's good intentions. Although the report remains a secret document, it is believed to have concluded that the Chinese economy could make up the resulting reduction in foreign currency without much hardship.⁶⁹ Chinese officials indicated that the report went to such an extreme that "China might actually benefit from cutting out Hong Kong because it would have to share local profits of international trade with local capitalists, high priced Hong Kong workers and foreign investors."⁷⁰

64. *Id.* Some bankers view supervision of currency and banking affairs as an essential element of national sovereignty, which Beijing has stated it will recover and use over Hong Kong, and may interfere in either Hong Kong's domestic or international economy. *Id.*

65. See *supra* notes 46-49 and accompanying text.

66. *The Crucial Confidence Factor*, *supra* note 48.

67. Thomas Ivanyi, a Citibank vice president, expressed Chinese Hong Kongers' mistrust in their precautionary behavior. "Take someone from Shanghai who rebuilt himself in the 1950s and 1960s . . . As soon as he had two dollars, he thought of keeping one abroad, of keeping funds in Switzerland." *Id.* See also *The Art of Staying Central*, *supra* note 63, at 164.

68. *The Art of Staying Central*, *supra* note 63, at 166.

69. *Id.*

70. *Id.*

Pessimists will also point out that much of Hong Kong's prosperity is due largely to Britain's non-interventionist policies.⁷¹ With the future largely in China's control, Hong Kong's government will be considerably less non-interventionist.⁷² This shift away from non-interventionist policy is expected especially when one takes into consideration that the Chinese agencies presently on the island will expect to be heard from in the future more than they have been in the past. Thus, Hong Kong's established administration will have to take a strong stand in order to preserve its authority.⁷³

Of particular interest is the question of how much capital China has already invested in Hong Kong. Although the exact amount is not known,⁷⁴ one economist has assessed China's direct investment in Hong Kong property, manufacturing and services to be at least six billion dollars.⁷⁵ This amount would account for at least one third of all direct foreign investment in Hong Kong,⁷⁶ thus, "[i]n a way China has already reclaimed Hong Kong."⁷⁷

This reclamation is of even greater significance given the fact that many lower level Chinese officials believe that China should not hesi-

71. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 5.

72. *Id.* Reflective of this occurrence is a comment by a managing director of a Hong Kong financial institution who stated that it is not unusual that after setting up a "big" deal with Singapore or Malaysian money "[a]t the last minute the Chinese authorities cable to change the terms laid down in the documentation, and you say: we don't need this, it doesn't happen anywhere else." Goodstadt, *Hong Kong Builds Bridges to China*, *EUROMONEY*, Apr. 1985, at 158.

This frustration in conducting business transactions is largely the result of the problem that Chinese commercial law is not as well developed as in the western nations. *Business, Business, Business* . . . , *THE ECONOMIST*, May 11, 1985, at 20. The root of the problem has been summarized as follows:

China is establishing a code of commercial law, but it is a slow business that proceeds through the publication of foreign-investment rules that are more in the nature of guidelines than comprehensive legal enactments. Foreigners complain that on issues such as compensation for breach of contract, the resolution of disputes and the remittance of foreign exchange, China's law is too vague. Getting it right matters not just for China and its foreign partners, but also for Hong Kong's future. One of the advantages Hong Kong now has is its internationally accepted commercial law. More than just businessmen will be watching how China learns to live with a western legal system.

Id. at 18.

73. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 5.

74. The exact amount is unknown because the Hong Kong Government omits China from its foreign investment statistics for the colony out of fear of frightening local businessmen. *Business, Business, Business* . . . , *supra* note 72, at 20.

75. *Id.* (the article does not state whether this is HK or US dollars).

76. *Id.* (the United States is the only other country that comes even close to matching this amount of direct investment).

77. *Id.*

tate to take "direct advantage" of the situation in light of the fact that Britain has conceded that Hong Kong will become a Chinese territory in 1997.⁷⁸ Senior officials in the Chinese Communist Party realize that such a strategy would jeopardize the increasing international confidence in Hong Kong's long term survival.⁷⁹ Although China has not attempted to take "direct advantage" of its status as sovereign, it has, nevertheless, begun to send a clear message to Britain and Hong Kong that Beijing is closely watching the development of the colony's political system.

What has most damaged the current state of affairs among China, Hong Kong and Britain has been the attempts by the Hong Kong Government to pass a number of political reforms that would increase representation of the Hong Kong people. On September 26, 1985, Hong Kong held its first indirect elections for seats on the Legislative Council (Legco), the Island's advisory law making body.⁸⁰ These indirect elections were conducted under an electoral college system.⁸¹ Soon after these elections, Hong Kong's Chief Secretary, Sir David Akers-Jones, stated that the Hong Kong government is not required to consult Beijing on how the territory is to be administered during the transitional period ending in 1997.⁸² At this time, political activists close to Hong Kong's Governor, Sir Edward Youde, took the opportunity to urge that direct elections on a one-man, one-vote basis should be introduced for a certain percentage of the Legco seats in 1988.⁸³ If permitted, it is hoped that such a voting scheme will be incorporated by drafters into the Basic Law.⁸⁴

Although China did not interfere with Legco's indirect elections, China still fears that a more representative legislative body could evolve into a powerful local government⁸⁵ which may become so independent by 1997 that the people of Hong Kong will not want to return to China.⁸⁶ Implicit in this fear is Beijing's reiteration of its "objection

78. *Id.*

79. *Id.*

80. E. Lau, *The Buck Stops Here*, FAR E. ECON. REV., Oct. 17, 1985, at 28, col. 1.

81. *Id.*

82. *Id.*

83. *Id.* Some officials have talked of having twenty-five percent of Legco's seats filled by direct election in 1988. J. Burns, *Hong Kong Has Seen the Future and Has Doubts*, N.Y. Times, Jan. 7, 1986, at A2, col. 5.

84. *Id.*

85. J. Wong, *Hong Kong Jolted as China Attacks Political Reforms*, Asian Wall St. J., Dec. 2, 1985, at 24, col. 3.

86. E. Lau, *Laying Down The Law*, FAR E. ECON. REV., Dec. 5, 1985, at 14, col. 1. China does not want to face a situation where Hong Kong's democratization would reach such a level that Britain "can disclaim responsibility and say they can no longer influ-

to the concept of the Hong Kong government 'returning the administration to the people.'"⁸⁷ China's concern has arisen as a result of its view that sovereignty and administration are inseparable.⁸⁸ One senior Chinese official has commented that such representation is a "retrograde step from the joint declaration."⁸⁹ Even some "unofficials" (non civil servants) presently sitting on Legco have expressed their reservations about direct elections. To this group of "unofficials" a high degree of autonomy "is not synonymous with independence, nor with the freedom of action one normally associates with democratic government based on universal suffrage."⁹⁰

China's tolerance, in taking a passive stance in permitting political reforms to occur without its consultation, came to an abrupt end in late November 1985. In a highly unusual press conference, China's chief spokesman in Hong Kong, Xinhua news agency director, Xu Jiatun, clearly enunciated Beijing's position that all political reforms concerning the Hong Kong government should be halted until the Basic Law comes into force in 1990.⁹¹ In condemning the Hong Kong administration's efforts to develop more direct representation within the government, Mr. Xu declared that such policies were the result of Britain's "current tendencies to deviate from [the Joint Declaration]" and suggested that such deviations would cause "unfortunate" consequences for the colony.⁹² Governor Youde's only comment was that he was unaware of any breaches in the Sino-British agreement.⁹³

Thus, the issue of political representation has become the first challenge to the Joint Declaration's ability to resolve political conflicts. It is essentially the first time that the two signatories have differed considerably on the interpretation of the agreement's meaning. Britain has forcefully argued that a clause in the agreement directs that the colonial administration will be responsible for local affairs until 1997.⁹⁴

ence localised legislators." *Id.* at 13, col. 3.

87. E. Lau, *supra* note 80, at 28, col. 3.

88. *Id.*

89. *Id.*

90. E. Lau, *Consent to Concession*, FAR E. ECON. REV., Dec. 12, 1985, at 21, col. 3.

91. E. Lau, *supra* note 86, at 12, col. 1.

92. J. Wong, *supra* note 85, at 1, col. 2.

93. *Id.*

94. *Id.* Britain no doubt is referring to the clause of the Joint Declaration which states:

The Government of the United Kingdom and the Government of the People's Republic of China declare that, during the transitional period between the date of the entry into force of this Joint Declaration and 30 June 1997, the Government of the United Kingdom will be responsible for the administration of Hong Kong with the object of maintaining and preserving its economic prosper-

Britain's position is that any reforms before 1997 are quite simply none of China's concern. China, on the other hand, has stated that it is up to the SAR, under Chinese leadership, to evolve the system of political reform.⁹⁵

Britain's actual position, however, is evidenced by the events which followed the publication of China's displeasure regarding the movement for direct elections.⁹⁶ Hong Kong's Chief Secretary, Akers-Jones, retracted his earlier statements,⁹⁷ declaring that the "Hong Kong Government will inform Beijing of any proposals for political reforms in 1987 before they are made public here."⁹⁸ The Chief Secretary also mentioned that a "green paper," or consultative document, concerning reforms would soon be given to the People's Republic.⁹⁹ Trying to save face, the Chief Secretary added that the "green paper" would result only in an "exchange of views" between Hong Kong and Beijing, but that Hong Kong would not be consulting China.¹⁰⁰

The net effect of the "green paper exchange" is of great importance when examining the power struggle over grooming Hong Kong for 1997. Essentially, it has confirmed the Hong Kong people's impression that although Britain had claimed it would resist China's interference and not be "mere caretakers for the next 12 years,"¹⁰¹ it is apparent that Britain lacks the "political will" to stand up to Chinese pressure.¹⁰² More importantly, Britain's submission to China's demands has given Beijing a veto power over political reforms through the transition period ending in 1997.¹⁰³

Only one week after Xu Jiatur's controversial press conference a second major political volley was underway. Pro-Beijing elements in the Basic Law Consultation Committee's (BLCC) standing committee were accused of introducing "a communist style electoral process" into the election of seven BLCC "office bearers."¹⁰⁴ The BLCC constitution

ity and social stability; and that the Government of the People's Republic of China will give its cooperation in this connection.

Joint Declaration, *supra* note 1, at para. 4.

95. E. Lau, *Telling Big Brother*, FAR E. ECON. REV., Jan. 16, 1985, at 37, col. 1.

96. See *supra* notes 91-93 and accompanying text.

97. See *supra* notes 80-82 and accompanying text.

98. E. Lau, *supra* note 95, at 37, col. 1. Akers-Jones agreed with a high ranking Chinese official that "no major political changes should be made in the transition period." *Id.*

99. *Id.*

100. *Id.*

101. E. Lau, *supra* note 86, at 13, col. 2.

102. *Id.*

103. E. Lau, *supra* note 95, at 37, col. 1.

104. E. Lau, *Haste Makes Waste*, FAR E. ECON. REV., Dec. 19, 1985, at 14, col. 1

sets forth the requirements to elect its office bearers. Accordingly, the seven office bearers "shall be elected among members of the standing committee."¹⁰⁵ The standing committee, however, ignored the BLCC constitution, thus violating the territory's rule of law, when four vice-chairmen of the Basic Law Drafting Committee (BLDC)¹⁰⁶ proposed seven names to fill the seven posts.¹⁰⁷ The proposal was seconded by one of the nominees.¹⁰⁸ There were no objections, and the seven were immediately installed.¹⁰⁹

As was to be expected, three BLDC members who had been involved in drafting the BLCC constitution objected to how the elections were conducted. They stated that "the selection of the office bearers was un-constitutional because the four BLDC vice-chairmen had no mandate to propose them."¹¹⁰ In calling for a new election, one Legco "unofficial" stated that, if required, any member of the BLCC could seek a court order declaring that the election was unconstitutional, thus voiding the result.¹¹¹ Xu Jiatun defended the election process saying that the seven office bearers were selected "by election through consultation," and that this form of consultation is but one form of election.¹¹²

[hereinafter E. Lau, *Haste*]. The BLCC's function is to collect public opinion in Hong Kong on the Basic Law. Its 180-member body consists entirely of local people. The standing committee is its executive arm. *Id.* Due to its large size and the diversity of its members, the BLCC portrays an image of wide representation. However, it is already rumored that the BLCC may be dominated by a powerful and united pro-Beijing faction which in essence turns it into a rubber stamp. E. Lau, *Peking Honours List*, FAR E. ECON. REV., Dec. 5, 1985, at 13, col. 2.

105. E. Lau, *Haste*, *supra* note 104, at 14, col. 2. The standing committee consists of 19 members elected from among the BLCC's general members. *Id.* at 14, col. 1.

106. The BLDC is a 59-member body appointed by Beijing to draft the Basic Law. The Hong Kong interest is represented by 23 natives out of the 59 seats. E. Lau, *Advise Before Consent*, FAR E. ECON. REV., Jan. 2, 1985, at 10, col. 2. Compare A. Ignatius, *Hong Kong's Premier Capitalist Roaders Are Emerging as Peking's Trusted Allies*, *Asian Wall St. J.*, Jan. 27, 1986, at 16, col. 2 (25 of the 59 seats are held by Hong Kong natives). The BLDC's chairman is a communist party official. *Id.*

107. E. Lau, *Haste*, *supra* note 104, at 14, col. 2. One of the vice-chairmen of the BLDC happened to be Xu Jiatun. Jiatun, in the previous week, had accused Britain of deviating from the Joint Declaration. *Id.* at 14, col. 1; see also E. Lau, *supra* note 86, at 12, col. 1; J. Wong, *Hong Kong Jolted As China Attacks Political Reforms*, *supra* note 85, at 1, col. 5.

108. The nominee who seconded the proposal was Ti-liang Yang, a High Court judge. E. Lau, *Haste*, *supra* note 104, at 14, col. 2.

109. *Id.*

110. *Id.* at 14, col. 3.

111. *Id.*

112. *Id.* Xu went so far as to say that the drafters of the BLCC constitution had wanted to use the term "consultation" instead of "election," but chose not to because

A "proper" BLCC standing committee meeting was promptly convened in which it was agreed that the elections of the previous week violated the BLCC constitution.¹¹³ New elections were held with the original seven names again being nominated and re-elected by a show of hands.¹¹⁴

Understandably, the events discussed have seriously shaken the public's confidence that Hong Kong's future will remain anywhere near as free and autonomous as the Joint Declaration sets forth.¹¹⁵ With regard to Mr. Xu's press conference, his comments are believed by some to have damaged China's international reputation.¹¹⁶ One retired senior colonial administrator stated that Xu's message confirmed Hong Kongers' suspicions that "the Sino-British agreement isn't worth the paper it's written on unless Peking keeps its word."¹¹⁷ The chairman of Meeting Point, a pro-Beijing political organization, expressed that the BLCC affair damaged its reputation and independence, and weakened the Hong Kong people's faith in the rule of law and democracy, thus seriously undermining public confidence.¹¹⁸

In order to quash the territory's worst fears, Beijing promptly sent Ji Penfei, a Chinese state counsellor and director of Beijing's Hong Kong and Macao Affairs Office to "repair the damage without giving

some in Hong Kong objected. *Id.* It is unfortunate for Xu that he did not stop to think and realize that the three BLDC members who drafted the BLCC constitution were alive and well but expressed no such intention concerning the choice of words. In fact, one of the drafters of the BLCC constitution publicly condemned the selection of the seven office bearers as unconstitutional. *See supra* note 110 and accompanying text.

113. E. Lau, *Haste*, *supra* note 104, at 15, col. 2.

114. *Id.*

115. *See supra* notes 50-54 and accompanying text.

116. J. Wong, *supra* note 85, at 24, col. 2; *see also supra* notes 91-93 and accompanying text.

117. *Id.* One BLDC vice-chairman expressed concern to Ji Pengfei, a Chinese state councillor and director of Beijing's Hong Kong and Macao Affairs Office, that such statements by Xu must be curbed, warning that "millions of dollars could be shipped out of Hong Kong via a simple telex by anyone worried about Hong Kong's political stability at any given time." E. Lau, *supra* note 106, at 10, col. 3.

118. E. Lau, *supra* note 86, at 15, col. 3. Another political group, the Hong Kong Observers, wrote to Ji Pengfei that "[t]he action of the vice-chairman has caused a lot of people in Hong Kong to suspect that Peking has already made up its mind on the details of the future Hong Kong system. If that is the case, then the setting up of the drafting committee and consultation committee would only be part of a charade, with little impact on the ultimate contents of the basic law." E. Lau, *supra* note 106, at 11, cols. 1-2. Public confidence was not boosted when at the same time of the unconstitutional selection of the seven BLCC office bearers, six BLDC were selected to the BLCC. This was seen as an "undisguised attempt to dominate BLCC hearings. In so doing, the BLDC could be accused of consulting with itself." E. Lau, *supra* note 86, at 15, col. 3.

anything away."¹¹⁹ An indication of China's understanding of the impact of Mr. Xu's statements and the void BLCC election is evidenced by the fact that Ji is the highest ranking Chinese official to visit Hong Kong since 1949.¹²⁰

Along with Ji's visit it was made known that Beijing is considering allowing 60 percent of Legco's seats to be directly elected.¹²¹ This would be conditioned upon concentrating power in the chief executive who would be advised by a 100-member executive advisory council composed of mostly local capitalists.¹²² Though Ji's visit seems to have quieted the political climate, the damage has been done and it is not so easily removed. The Island will continue conducting its affairs until the next bite is taken out of its autonomy by Beijing.

Although the fears of the pessimists are persuasive and can not be dismissed as mere fantasy, there are overwhelming indications that the economic recovery Hong Kong is experiencing is not based on false pretense or misguided speculation.

B. The Optimists

Businessmen have continued to maintain that there is a profitable future for their private enterprise in Hong Kong.¹²³ "Here money speaks."¹²⁴ Only two months after the signing of the accord on December 19, 1984, the Hang Seng market index had increased by 15% to its highest level in two-and-a-half years.¹²⁵ Exemplifying the market's volatility was its immediate drop of almost 50 points the day after Xu's accusation that Britain was deviating from the Joint Declaration.¹²⁶ Characteristically, the Hang Seng index rebounded in a frenzy. Only six weeks after the sudden drop, the Hang Seng closed at a new record high in its history.¹²⁷

119. E. Lau, *supra* note 106, at 10, col. 2.

120. *Id.* at 10, col. 1.

121. *Id.* at 11, col. 1; compare *supra* note 83 and accompanying text.

122. *Id.* at 11, col. 1.

123. Finer, *Hong Kong 1997: When the Kissing Has to Stop*, 56 POL. Q. 262, 265 (1985).

124. *Id.*

125. Elliott & Jones, *A Bullish Outlook for the Year of the Ox*, BUSINESS WEEK, Feb. 4, 1985, at 43; compare *Deng and the Dollar Rend Hong Kong Assunder*, 292 ECONOMIST 71 (July 14, 1985) (the first two weeks in July, 1984 saw the Hong Kong index have its sharpest decline).

126. E. Lau, *supra* note 86, at 15, col. 2; see also *supra* note 91 and accompanying text.

127. *Hang Seng Soars to Record, But Rumors Force Retreat*, Asian Wall St. J., Jan. 13, 1986, at 27, col. 1. The record high was set at 1826.84 on Wednesday, Jan. 8, 1986. The Hang Seng's previous market record of 1810.2 was set back on July 17, 1981. *Id.*

In January 1985, two corporate transactions of major significance occurred. First, Hutchinson Whampoa, Hong Kong's only Chinese "hong,"¹²⁸ acquired control of Hong Kong Electric from the Hong Kong Land Company. Second, a joint venture contract was signed between China Light & Power and Beijing to build China's first nuclear power plant. Both transactions were the work of two of Hong Kong's most powerful taipans,¹²⁹ and reflect their confidence in and optimism for the Sino-British accord.¹³⁰

Perhaps the most valid indicator of the present mood of investment in Hong Kong is in land sales and office space sales. Land investment has increased since the real estate market collapse in 1981-1982.¹³¹

An improvement in the residential property market is a result of the return of a vast number of people who had previously emigrated from Hong Kong.¹³² Due to this, vacancies in private domestic premises are falling.¹³³ This comes as good news for developers and traders and "important for Hong Kong's stock market which is ironically dominated by property companies."¹³⁴

Even more indicative of the growing strength of Hong Kong's economy is the decline in available office space. Although the market

128. A "hong" is a commercial establishment or house of foreign trade. WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 1086-87 (1981).

129. "Taipan" is from the Chinese word for "big boss." Singer, *The Taipans of Hong Kong*, CHINA BUS. REV., Sept.-Oct. 1985, at 38.

130. *The Era of the Bull*, ASIAN FIN., Mar. 15, 1985, at 40. The acquisition by Hutchinson Whampoa of Hong Kong Electric involved the single largest check ever to change hands in Hong Kong's corporate history. Li Ka-shing, chairman of Hutchison, may have conducted the transaction in such a manner as a symbolic gesture "to tell the world that everything is going to be all right with Hong Kong." *Id.* It might be added that as a result of Li Ka-shing's recent acquisitions, he now controls four companies whose combined capitalization accounts for nearly 10 percent of Hong Kong's entire stock market. Elliot & Jones, *Hong Kong's Li Ka-shing Puts His Money Where His Mouth Is*, BUSINESS WEEK, Feb. 4, 1985, at 44. It is no wonder that Li, with holdings so large in Hong Kong, is committed to Hong Kong's future and wants to portray a climate of stability for investment. One must keep in mind, however, that he further committed himself with the acquisition of Hong Kong Electric after the signing of the Sino-British accord, reflecting a true capitalist spirit of confidence in Hong Kong's future. Li wields such influence in the Hong Kong business community that his latest moves were expected to set off a stock-buying stampede. Elliot & Jones, *supra* note 125, at 43.

131. See *Hong Kong: With Agreement Confidence Returns to Office Market*. 27 INT'L REAL EST. INVESTOR 54 (Jan. 1984); *Era of the Bull*, *supra* note 130, at 42-43.

132. *Era of the Bull*, *supra* note 130, at 42.

133. Apartment sales reached an all time height in 1985. According to the Registrar General's Office, 54,405 apartments were sold in 1985, an increase of 81.6 percent. *Hong Kong Business Briefs*, Asian Wall St. J., Jan. 20, 1986, at 13, col. 2.

134. *Era of the Bull*, *supra* note 130, at 42.

for commercial office space is still in oversupply, realtors are not overly concerned because, as one international real estate firm stated, "[t]he demand is increasing in Central [downtown] for prime office space, and there's no new large office building coming up over the next two or three years."¹³⁵ Some realtors are predicting that there might in fact be a shortage of office space by 1988-1989 which would drive rents higher.¹³⁶

Construction is also experiencing a healthy rebound. Hong Kong Land Company¹³⁷ has already decided to add a third tower to its Exchange Square complex, predicting with confidence that there will be a "firming up of demand" to absorb the newly created space.¹³⁸ Hutchinson Whampoa has given the go-ahead on a 94-story residential and commercial development on Kowloon's waterfront which will be the biggest development ever undertaken in Hong Kong.¹³⁹ Hutchinson's director, Mr. Li, has full faith that the "property market is now at its lowest and will pick up on its own momentum."¹⁴⁰

On September 24, 1985, the first government land auction took place under the Joint Declaration and was hailed as a success.¹⁴¹ The six lots involved were the first sold in the New Territories with leases that extend beyond 1997, and for which the proceeds will be divided, as pre-determined by the Joint Declaration between China and the government of Hong Kong.¹⁴² Sir Edward Youde, Governor of the Island, said the land sales are evidence that "the Agreement on the future of Hong Kong has stood the test . . . in the first year," and added that "the Agreement is going into effect and steady progress will be made to put into effect all the arrangements in it."¹⁴³

135. *Id.* at 44.

136. *Id.* The Bank of China has begun construction on its Hong Kong branch building which is to become Hong Kong's tallest structure by far. This symbolic gesture in "concrete and curtain walls" may reflect China's commitment to preservation of Hong Kong's economy. *Business, Business, Business* . . . , *supra* note 72, at 20.

137. The Hong Kong Land Company is the largest single land holder in Hong Kong today. *Hong Kong Land Plans A Commercial Paper Issue Of \$128.5 Million*, *Asian Wall St. J.*, Oct. 21, 1985, at 30, col. 4.

138. *Era of the Bull*, *supra* note 130, at 44.

139. *Id.*

140. *Id.*

141. *Hong Kong's Auction of Land Successful*, *Pacific Basin*, Sept. 25, 1985, at A5, col. 5; Letter from the Commissioner of Hong Kong Commercial Affairs to Members of the Hong Kong Association (Nov. 1985) (available at the Hong Kong Commissioners Office, New York City).

142. *Hong Kong's Auction*, *supra* note 141, at 5A, col. 6. (A Hong Kong government agent said that the "sales have not shown massive increases that could indicate a boom [but] the steady rise and strength of the market.").

143. Telex from DIS to the Hong Kong Trade Commissioner, New York City (Sept.

From the previous discussion it becomes apparent that real estate investors, who were crippled and nearly destroyed during the collapse of the property market in 1981-82, would be one of the last investors to take expansive measures unless they had a firm conviction that Hong Kong's growth will continue.

Banking is another critical facet of Hong Kong's economy. Due to the large volume of business transactions that occur on the island, banking is big business. The current increase in the regulation of banking practices should provide improved security to business transactions and attract additional foreign investment.¹⁴⁴ It is widely believed that the strength of Hong Kong's banks is considered an essential protection against intervention by Beijing in Hong Kong's internal affairs.¹⁴⁵ It will, however, take a major effort from the banking community to provide this needed strength. The financial services available in Hong Kong did not develop as a result of government encouragement but rather because "financiers found it to be the right environment."¹⁴⁶

A recent market development exemplifies the financial community's innovative efforts to keep a step ahead of Beijing. In 1985, a Hong Kong Index futures contract will be introduced onto the financial market.¹⁴⁷ Designed primarily for local investors, it is hoped that a suc-

25, 1985).

144. In the past two and one half years the Hong Kong government has taken over three local banks which had failed primarily because of bad loans. Hye, *Hong Kong Secretly Backs Ka Wah With Public Funds*, *Asian Wall St. J.*, Feb. 3, 1986, at 4, col. 1. It is thus apparent that regulations are needed to prevent such liquidity problems and secure the confidence of the public in the Island's banking institutions.

On Jan. 8, 1986, the China International Trust and Investment Corporation, which is directly responsible to China's State Council, announced an "agreement in principle" to take over Ka Wah Bank. *Id.* at col. 2. Some have viewed the bail out of Ka Wah as a showing of Beijing's willingness to keep its promises to help maintain Hong Kong's stability and prosperity. *Id.*

145. Rooks, *China's Reunification Policy Shades Economics of Hong Kong, Taiwan*, *Oregonian Sun*, Sept. 1, 1985, at 3.

146. *The Art of Staying Central*, *supra* note 63, at 165. Fell, Hong Kong's banking commissioner, stated that financial authorities must give positive encouragement to new activities and institutions. "If Hong Kong is going to be more than just another manufacturing city in southern China we've got to get the financial centre right, and we've got limited time." *Id.* at 166.

147. Geraghty, *A Step Into The Financial Futures*, *ASIAN FIN.*, Mar. 15, 1985, at 74. "Conceptually, the stock index represents a diversified portfolio, and the provision of stock index futures may encourage equity holding by minimizing the risks posed by market fluctuations By definition, a stock index futures contract is a commitment to participate in the overall price movement of the stock market as measured by some underlying stock index." *The Mechanics of Stock Index Futures*, *ASIAN FIN.*, Mar. 15, 1985, at 76 (see this article for an example of a practical application of the futures contract).

cessful futures contract will open the door to other new futures contracts based on gold, currencies and financial instruments, which would add further depth to Hong Kong's financial center.¹⁴⁸

Aside from Hong Kong's banking and financial institutions, it possesses one resource essential to any capitalist infra-structure—people. In the long run, Hong Kong's greatest asset may be its people. The labor force, which is intelligent and well-trained, is able to adapt to continual changes in industry.¹⁴⁹ This ability has contributed greatly to Hong Kong's economic success.¹⁵⁰ This is especially important considering the presence of a large number of light industries, where if one product is not successful the company may change the production line quickly to manufacture another product.¹⁵¹

There is some concern that the Sino-British accord might have a negative impact upon the middle class, a segment of the population upon which Hong Kong so regularly depends.¹⁵² The Nationality Act, which is derived from the Joint Declaration,¹⁵³ has instilled fears in many Chinese Hong Kongers that they might one day have to move again to avoid being subjected to a standard of living along socialist lines.¹⁵⁴ This is understandable since many emigrated to the Island to escape such socialist restraints on their lives.

Economically, China and Hong Kong are becoming increasingly interdependent. As a result, investors may lend greater credence to signals by the Central Committee of China's Communist Party that it will not only be more tolerant, but will actively seek liberal reforms in its economic structures.¹⁵⁵

148. Geraghty, *supra* note 147, at 74.

149. See *The Art of Staying Central*, *supra* note 63, at 166. One prominent financial investor has stated: "We're entering unknown territory, there isn't a precedent [but] I can't think of better people to venture into the unknown — entrepreneurial Hong Kong Chinese." *Id.*; see also *Reverse Takeover*, *ASIAN FIN.*, Mar. 15, 1985, at 47 (population able to constantly change from one industry to another). Cultural attributes such as a strongly ingrained work ethic and pursuit of excellence, as well as limited political aspirations under colonial rule, have helped make Hong Kong entrepreneurs extremely aggressive and dynamic. E. Chen, *Maintaining Hong Kong's Prosperity*, *CHINA BUS. REV.*, Sept.-Oct. 1985, at 7, col. 2. In addition, the absence of strong trade unions and minimum wage laws, and high labor mobility contribute to the Island's ability to maintain competitive wage rates in the world market. *Id.*

150. *Reverse Takeover*, *supra* note 149, at 47.

151. *Id.* at 46.

152. *Id.* at 47.

153. On Sept. 10, 1982, China decreed a Nationality Act which expressly rejects "dual nationality." S. Finer, *Hong Kong 1997: When The Kissing Has To Stop*, *POL. Q.* 262, 269 (1985).

154. *Reverse Takeover*, *supra* note 149, at 47.

155. See *supra* note 62 and accompanying text.

Growth in Hong Kong's domestic exports and re-exports to China are striking. Hong Kong's domestic exports to China grew from HK\$81 million in 1978 to HK\$11.3 billion in 1984, while re-exports grew from HK\$214 million in 1978 to HK\$28 billion in 1984.¹⁵⁶ This accounts for approximately one-half of all Hong Kong's re-exports.¹⁵⁷ Re-exports have resulted in a booming market since they are sold for more than the cost of importing them.¹⁵⁸ Similarly, China has increased its supplies to Hong Kong. In 1984, China's exports to Hong Kong reached over HK\$55.8 billion from only HK\$10.6 billion in 1978.¹⁵⁹ Also significant is China's move to becoming Hong Kong's second largest trading partner after being ranked only twenty-fifth in 1978.¹⁶⁰ Some observers warn that China's new open door policies might result in Hong Kong markets becoming overdependent on the mainland.¹⁶¹ In the first five months of 1985, Hong Kong's trade with China jumped forty-four percent compared to the same period in 1984.¹⁶² This accounted for more than a quarter of Hong Kong's total trade during this period.¹⁶³

Notice should also be taken of the recent movement towards protectionism by the industrialized countries of the world. Analysts have urged that now is the time Hong Kong should make the transition from labor-intensive to technological and capital-intensive export industries.¹⁶⁴ For example, when the United States Senate approved the Jenkins Bill on October 11, 1985, textile manufacturers in Hong Kong feared they would have much to lose.¹⁶⁵ The bill was to set limits on textile imports to the United States,¹⁶⁶ which incidentally happens to be Hong Kong's largest trading partner.¹⁶⁷ Thus, when President Reagan vetoed the Jenkins Bill on Dec. 10, 1985, government officials and industry leaders in Hong Kong were greatly relieved.¹⁶⁸ As Hong

156. C. Beckett, *Hong Kong's China Market*, CHINA BUS. REV., Sept.-Oct. 1985, at 41, col. 3.

157. *Protectionist Threats, Commodities Slump Clouds on Regions Trade Prospects*, Asian Wall St. J., Oct. 21, 1985, at col. 4 [hereinafter *Protectionist Threats*].

158. *Id.* (re-exports to all destinations in the first eight months of 1985 rose 37% to \$9.02 billion; those to China rose 140% in the first half).

159. *Id.*

160. *Id.*

161. *Id.* See also *supra* notes 68-77 and accompanying text.

162. *Id.*

163. *Id.*

164. E. Chen, *Maintaining Hong Kong's Prosperity*, CHINA BUS. REV., Sept.-Oct. 1985, at 37, col. 3.

165. *Protectionist Threats*, *supra* note 157, at 1, col. 3.

166. *Id.*

167. C. Beckett, *supra* note 156, at 41, col. 3.

168. *Hong Kong Government Information Services*, WEEK IN HONG KONG, No. 50/85 (Dec. 16-22, 1985).

Kong's overall domestic export market is declining¹⁶⁹ such threatening protectionist measures are increasingly causing more concern than similar international moves did in 1982.¹⁷⁰ In the long run, it would appear that Hong Kong's comparative advantage in traditional exports is becoming exhausted and it is essential that its "comparative advantage in technology and capital (both human and physical) intensive industries" be realized.¹⁷¹

Moreover, in geo-political terms, China needs to assure Hong Kong's future economic stability in order for China to attain the "crown jewel"¹⁷²—Taiwan.¹⁷³ Conceivably, Beijing's "ultimate goal of reunification with Taiwan" will be heavily weighed when analyzing its commitments to Hong Kong.¹⁷⁴ To do otherwise would not only endanger Hong Kong's prosperity, but would reconfirm Taiwan's already settled perception of the faults of Communist rule.¹⁷⁵ Thus, the doctrine of "one country, two systems" was devised by Deng Xiaoping to justify tolerance of Hong Kong's capitalist system coexisting with China's socialist system, and can also be viewed as an offer directed to Taiwan.¹⁷⁶

As China's leader,¹⁷⁷ Deng Xiaoping is the central figure in nurturing the international business community's confidence in the stability of Hong Kong's markets and land values. Deng has also been the fore-

169. In the first eight months of 1985, domestic exports dropped 6.2% from a year earlier to \$10.77 billion. *Protectionist Threats*, *supra* note 157, at 22, col. 4. Domestic exports for the year ending 1985 fell 5.8 percent, the greatest yearly decline in domestic shipments since such statistics have been available (1964). A. Ignatius, *supra* note 31, at 16, col. 2. The decline in domestic exports was largely attributed to a decline in United States demand and curbs on China's imports. *Id.*

170. *Protectionist Threats*, *supra* note 157, at 22, col. 4.

171. E. Chen, *supra* note 149, at 40, col. 3. Hong Kong's "comparative advantage" refers to its versatile work force and competitive wages (*see supra* notes 149-51 and accompanying text) and the readily available sources of funds and technology. E. Chen, *supra* note 149, at 37.

172. Hsiung, *The Hong Kong Settlement: Effects on Taiwan And Prospects For Peking's Reunification Bid*, 12 *ASIAN AFFAIRS* 47, 49 (1985).

173. The Taiwanese government calls itself the Republic of China and considers itself the true Chinese government that controlled the mainland until the Communist insurrection drove it to Taiwan in 1949. *Id.* at 51. As a matter of interest, Taiwan currently possesses the original copies of the three nineteenth century Sino-British treaties. *See supra* notes 12-16 and accompanying text.

174. Hsiung, *supra* note 172, at 57.

175. *Id.* In anticipation of Hong Kong's return to China's sovereignty, Taiwan is to remove its presence from Hong Kong by 1997 in order to make reunification more difficult and unlikely. *Id.* at 53.

176. *Id.* at 50.

177. Deng is currently chairman of the party and state military commissions, and the party's central advisory commission. V. Fung, *Deng Paves Way for a Smooth Succession In China, Hoping to Keep Policies Alive*, *Asian Wall St. J.*, Jan. 20, 1986, at 6, col. 2.

runner in China's political movement towards a more capitalistically oriented socialism.¹⁷⁸ Lord Kadoori, one of Hong Kong's leading taipans, has stated that Deng told him in confidence that "though China would remain a socialist government, it realised fully the need for modernizing, and that . . . they would use capitalism to improve socialism."¹⁷⁹

Deng, having reached the young age of 81, realizes that upon stepping down he must leave behind a communist party that will continue his regime's acceptance of western economic concepts. Thus, Deng has given high priority to the succession issue.¹⁸⁰ In this vein, Deng recently ousted nearly one-third of the present military and political establishment and replaced them with sixty-four younger and better educated people who are perceived to be more technically competent.¹⁸¹ Realizing that the issue of succession is crucial to the future of his open-door policies and economic liberalization, Deng has already arranged for an orderly transfer of power to Hu Yaobang, the party Secretary-General, and Zhao Zeying, the Prime Minister.¹⁸² If Deng steps down from power in 1987 as has been rumored, Mr. Hu and Mr. Zhao would jointly run China.¹⁸³ Of course, this alone does not assure that the young and college educated successors will continue Deng's trend toward a more market oriented economy and away from the traditional

178. Deng has been the driving force behind China's new Open Door policies. See generally Selk, *Economic Scene: The Open Door Policy In China*, N.Y. Times, Sept. 27, 1985, at D2, col. 1. Deng's open door policy has opened up four Special Economic Zones, which include fourteen cities that will serve as a "window" for observing contemporary capitalism. *Id.*

179. *Reverse Takeover*, *supra* note 149, at 47.

180. V. Fung, *supra* note 177, at 6, col. 1.

181. Selk, *supra* note 178, at D2, col. 1; Goldman, *The Chinese Take An Economic Step*, N.Y. Times, Sept. 24, 1985, at A31, col. 5. ("Mr. Deng is putting young experts in positions of power in hope that they will continue to encourage his policies after he is gone").

182. V. Fung, *supra* note 177, at 6, col. 1.

183. *Id.* Much to his dismay, Deng Xiaoping's plans for an orderly transfer of power to Hu Yaobang have been completely dismantled. On Jan. 16, 1987, Mr. Hu, the leader of China's Communist Party, was forced to resign after being accused of "mistakes on major issues of political principles" during his tenure. Gargan, *Leader of Party in China is Ousted for His Mistakes*, N.Y. Times, Jan. 17, 1987, at A1, col. 6. Prime Minister Zhao Ziyang was appointed to temporarily replace Mr. Hu as acting general secretary of the party. *Id.* It is not clear at this time whether Mr. Hu's removal was motivated by Mr. Deng or forced by the party's old conservative block. Many academic specialists view Mr. Hu's removal as undermining the succession process which Mr. Deng so laboriously set in place. Butterfield, *Hu's Ouster: Deng's Role*, N.Y. Times, Jan. 17, 1987, at A1, A4, col. 6, 2. It was, however, also reported that Mr. Hu's removal was possibly the result of serious disagreements between he and Mr. Deng and that "Deng decided Hu wasn't up to his shoes." Butterfield, *supra* at A4, col. 3; Gargan, *supra* at A4, col. 5.

Soviet model of centralized planning and heavy industry.¹⁸⁴

There remains pressure from Deng's opposition not to follow, in their view, a radical departure from the old Maoist ways. A powerful conservative coalition remains in the Politburo which does not favorably view Deng's economic position.¹⁸⁵ Considering that some of these more influential opponents are "youths" themselves as compared to Deng, they may very possibly outlast Deng and return the Politburo to its more conservative economic policies of the past.¹⁸⁶ Observers note, however, that before Deng relinquishes his party posts he will have persuaded members of the "conservative old guard" to retire, thus removing any conservative challenges.¹⁸⁷

It seems that the political climate has mainly affected the investments of local, not foreign, investors. A general manager of a Hong Kong bank said that though confidence in short term investment has revived "it is the foreigners who have been more comfortable with the political risk than the local Chinese entrepreneur."¹⁸⁸ Thus, a great unknown of the coming years is whether the local Hong Kong Chinese business community will take heed of foreign investors continuing investment in Hong Kong, or liquidate Hong Kong holdings overseas.¹⁸⁹

IV. CONCLUSION

The signing of the Sino-British Joint Declaration in December 1984 marked the beginning of a new political and economic era for Hong Kong. With investment cycles at only three to five years,¹⁹⁰ it will be up to the business community and governments involved to sta-

184. Goldman, *supra* note 181, at A31, col. 5.

185. *Id.* This "inner circle" has "criticized such Western thinkers as Sarte, Freud, Kafka and the Eurocommunists for leading China's youth astray." *Id.* at A31, col. 6.

186. See generally Goldman, *supra* note 181, at A31, col. 5. Deng may also field opposition from the army which is not benefitting from the fruits of economic reform. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 4. One prominent Hong Kong businessman described succinctly that "[i]f Deng Xiaoping drops dead or the army, which has been pushed aside a bit in China, makes a come back, we might have a backhander." *The Crucial Confidence Factor*, *supra* note 48, at 161.

187. *Id.* It has been reported that foreigners view the chances of China reverting to the unstable days of the Cultural Revolution as remote. This is due to Deng's reforms which have improved the standard of living as reflected by peasant income increasing eighty percent between 1981 and 1985, and an increase in grain output of twenty-six percent over the same period. Fung, *supra* note 177, at 6, col. 3.

188. *The Crucial Confidence Factor*, *supra* note 48, at 161 (this manager added that "Beijing has to convince the local entrepreneur that things won't change again the future"). *Id.*

189. *Id.* at 163; see also *supra* note 67 and accompanying text.

190. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 5.

bilize economic sentiment and assure a prosperous future for one of the world's largest markets.

The Joint Declaration is binding on both China and Great Britain, and has passed the first crucial tests of the administration of its provisions. Without question, the biggest test of the Agreement's long-term effect will rest on the viability of the Basic Law's final draft. The international community eagerly awaits its arrival.

Division over the future of Hong Kong seems to be based upon one's philosophical orientation and discipline. Optimists are found readily camped within business circles. While the business community bases its optimism on the political rhetoric of a binding agreement, it adds substance to its beliefs by increasingly investing capital in Hong Kong's real property and commercial markets. As a result, Hong Kong is experiencing a solid economic revival.

Pessimists, however, provide constant reminders to the business community of the political realities involved in drafting Hong Kong's Basic Law. If differences in interpretation of the Joint Declaration continue to develop with regard to how the Basic Law will be drafted and what interests will be protected, one can only speculate as to the differences that may arise when implementing the final draft of Hong Kong's new constitution in 1997. The business community must realize that no matter how non-interventionist any government may be, ultimately governments control economies based upon their political doctrines. Thus, it has been stated that if "China can barely run one system consistently for any length of time, what hope is there for two?"¹⁹¹

While optimists focus on economic statistics examining the interdependence between Hong Kong and China, pessimists look to Hong Kong's economic statistics en masse. It is probable that with regard to the fulfillment of the Joint Declaration's terms, the factors concerning economic interdependence may more accurately reflect Hong Kong's likelihood of future success as a world market.

Presently, both Britain and China have adhered to the Agreement in all of its essential terms. There is no indication that either party will behave otherwise in the future. China's investments on the Island make more tangible her "political good will" towards Hong Kong's capitalist system, and no one doubts that Britain will remove herself by 1997.¹⁹² If China continues its liberalized economic policies it will in time become increasingly dependent upon and accustomed to the economic advantages of capitalism. As each week passes, Hong Kong may reap small assurances of the soundness of its economic future, although

191. *Id.* at 3.

192. *More Fears Than Cheers In H.K.*, *EUROMONEY*, Apr. 1985, at 151.

quite possibly that picture might not be purely capitalistic.

For the remaining eleven years through 1997, and to a large degree for the fifty years hence, multinational businesses have reason to expect returns on their short term investments. Whether Hong Kong will remain a major financial market will depend on who is in power in Beijing in 1997.¹⁹³ At this time, the political climate is favorable and Deng Xio Peng is making certain, to the best of his ability, that the political and economic climate remains so, long after he has passed.

Leonard J. Turkel

193. *Perhaps, Perhaps, Perhaps* . . . , *supra* note 3, at 4.